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David L. Meier
Director
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September 3, 1997

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Mr. William F. Caton, Acting Secretary
Federal Communications Commission
1919 M Street, NW, Room 222
Washington DC 20554

In the Matter of:

Price Cap Performance Review
for Local Exchange Carriers

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)
)

CC Docket No. 94-1

Dear Mr. Caton:

Enclosed are an original and eleven copies plus two additional public copies of Cincinnati Bell Telephone Company's Reply to Opposition to its Petition for Reconsideration of the Fourth Report and Order in the above referenced proceeding. A duplicate original copy of this letter and attached Reply is also provided. Please date stamp this as acknowledgment of its receipt and return it. Questions regarding this Reply may be directed to Patricia Rupich at the above address or by telephone on (513) 397-6671

Sincerely,

David L. Meier

Enclosure

cc: James Schlichting, Chief, Competitive Pricing Division
International Transcription Services, Inc

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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SEP 3 1997

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of

Price Cap Performance Review
for Local Exchange Carriers

Access Charge Reform

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CC Docket No. 94-1

CC Docket No. 96-262

REPLY TO AT&T OPPOSITION TO PETITIONS FOR RECONSIDERATION

I. INTRODUCTION

On July 11, 1997 Cincinnati Bell Telephone ("CBT") filed a Petition for Reconsideration ("Petition") of the Fourth Report and Order in CC Docket No. 94-1. On August 18, 1997, AT&T filed an opposition to CBT's Petition. CBT submits this Reply to AT&T's opposition.

In its opposition AT&T contends that the Commission has previously rejected the concept of using a lower X-Factor for small and mid-size LECs and that CBT has not justified that a lower X-Factor is appropriate. CBT submits that AT&T has mistakenly interpreted the Commission's past decisions and that CBT's data does indeed support its request that the Commission reexamine the X-Factor for the elective price cap companies. Accordingly, the Commission should grant CBT's Petition and expeditiously undertake a more detailed analysis to determine the appropriate X-Factor(s) for the elective price cap LECs.

II. SEPARATE X-FACTOR IS APPROPRIATE FOR ELECTIVE PRICE CAP LECs

AT&T argues that because the Commission has previously rejected a separate X-Factor for small and mid-size LECs, it is appropriate to do so now. AT&T contends that because the Commission could not decide on the appropriate X-Factor for small and mid-size LECs, it is appropriate to force them to use the same X-Factor as the larger LECs. This may have been acceptable under the interim plan when all companies had multiple X-Factors to choose from,¹ but when moving to a plan under which companies do not have a choice of X-Factor, the Commission must adequately address the differences between the large LECs and the smaller carriers.

As CBT indicated in its Petition, the Commission has acknowledged that there are differences between the large LECs and the smaller LECs.² Several studies were presented in previous proceedings substantiating a lower X-Factor for several of the elective carriers. Furthermore, in its Petition in the current proceeding CBT demonstrated that the Commission's own methodology results in an X-Factor for CBT significantly below the Commission's 6.5 percent X-Factor derived from RBOC data. AT&T does not challenge the results of the CBT study or the fact that this calculation using the Commission's methodology continues to validate the results of CBT's and other previous studies.³ Instead, AT&T relies on selected prior

¹ This should not be construed to indicate that CBT supported the sharing associated with the various X-Factors in the interim plan. CBT believes that sharing is inappropriate in any price cap plan.

² See CBT Petition at footnotes 6 and 21.

³ These studies demonstrate the significant differences between the larger mandatory price cap LECs and the smaller/mid-size elective LECs.

Commission decisions to substantiate its call for a single X-Factor for all LECs, without considering the evidence presented in those and other proceedings which indicates that small and mid-size LECs cannot achieve the same productivity gains as the large carriers.

AT&T's contention that CBT makes no attempt to show that the results of CBT's study are representative of mid-size companies as a class or other elective price cap carriers misses the point. CBT did not assert that its X-Factor is appropriate for all elective companies. Rather, CBT stated the evidence from CBT's current study, its previous study, and studies submitted by other small and mid-size LECs provides a strong indication that a lower X-Factor is appropriate for these companies and, as such, asks the Commission to undertake a more detailed analysis to properly ascertain the appropriate X-Factor(s) for these companies. CBT submits that the Commission cannot ignore the overwhelming evidence on the record showing that many small and mid-size carriers cannot achieve the same productivity gains as the large carriers. Unfortunately, because of the difficulty associated with determining an appropriate X-Factor for these companies, the Commission has once again done this in its Price Cap Order, as has AT&T in its opposition.

The Commission's concern, reiterated by AT&T,⁴ that it would not be administratively feasible to establish separate X-Factors for the broad classifications of smaller, independent LECs is not sufficient reason to arbitrarily assign these carriers a 6.5 percent X-Factor. There are three alternatives for setting a more appropriate X-Factor for these LECs. One approach is to set a separate X-Factor for each individual company. Although this could be done, CBT

⁴ AT&T Opposition p. 6.

understands the Commission's concern that such an approach could be administratively burdensome.⁵ The second alternative is to establish a single X-Factor for the small/mid-size companies that is distinct from the X-Factor established for the large mandatory price cap companies. This X-Factor would be derived using data from the small and mid-size LECs. Although this alternative would be administratively simple, and would be better than requiring the small/mid-size LECs to achieve the same level of productivity growth as the large mandatory price cap companies, it would not take into consideration the heterogeneity among the elective companies. Instead, CBT recommends that the Commission develop a relatively small number of separate X-Factors for the small/mid-size companies based on various characteristics. This approach would recognize the heterogeneity of the small and mid-size LECs, while still maintaining much of the accuracy and administrative simplicity of the first two alternatives.

AT&T states that a single X-Factor will better replicate a competitive environment, but completely mischaracterizes the competitive outcomes. Nothing in economic theory says that all firms will have the same rate of productivity growth in a competitive market. On the contrary, one would expect less efficient firms to have greater incentives to cut costs rapidly. Indeed, cost cutting (improving efficiency) may be the only way that such firms can survive in a vigorously competitive environment. This reasoning suggests that elective price-cap LECs which already have lower costs (higher efficiency) should be assigned lower X factors -- precisely in order to replicate competitive outcomes.

⁵ In the Matter of Policy and Rules Concerning Rates for Dominant Carriers, CC Docket No. 87-313, Second Report and Order, (FCC 90-314), released October 4, 1990 at para. 118.

AT&T also cites CBT's recent decision to elect price caps as support for its argument that the Commission should not reexamine the productivity offset for the elective price cap LECs. As CBT stated in its Application for Special Permission⁶ and in its Petition, CBT did not agree with the 6.5% X-Factor when it elected price cap regulation. CBT is facing the same competitive pressures as the larger price cap LECs. As the Commission has stated, the access charge reform order "will foster competition and economic growth by creating an access charge system that is economically efficient, fair, and compatible with competition."⁷ However, in order to be able to avail itself of the new economically efficient levels and rate structures adopted in the access reform order,⁸ CBT had to elect price cap regulation because the Commission concluded that most of the access charge reforms "should be limited to price cap incumbent LECs."⁹ The Commission concluded that most of the non-price cap LECs were unlikely "to face significant competition in the immediate future"¹⁰ and therefore, a separate proceeding would be conducted at a later date to address their concerns. Contrary to the Commission's conclusion, CBT is

⁶ CBT Application No. 118, filed June 13, 1997.

⁷ "Commission Reforms Interstate Access Charge System," Report No. CC 97-23, FCC News Release, May 7, 1997. Also see In the Matter of Access Charge Reform, CC Docket No. 96-262; Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1; Transport Rate Structure and Pricing, CC Docket No. 91-213; End User Common Line Charges, CC Docket No. 95-72, First Report and Order, (FCC 97-158), released May 16, 1997 (hereafter "Access Reform Order") at paras. 13-16.

⁸ While CBT clearly needs the access reforms afforded the price cap carriers in the Access Reform Order, CBT believes that certain actions taken by the Commission in that proceeding were unreasonable and/or unlawful and, therefore, has sought judicial review of the Access Reform Order. See, CBT's Petition for Review of the Access Reform Order, filed August 8, 1997 in the United States Court of Appeals for the Sixth Circuit.

⁹ Access Reform Order at para. 330.

¹⁰ Access Reform Order at para. 331.

facing immediate competition and could not wait until the Commission completed another proceeding to address its need for a more cost causative access charge structure.

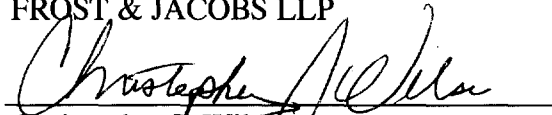
III. CONCLUSION

For the reasons described above, CBT submits that AT&T has not presented any convincing evidence for why CBT's Petition should be denied. CBT maintains that the evidence presented in its Petition continues to support reconsideration of the X-Factor as it applies to elective price cap LECs and encourages the Commission to expeditiously undertake the analysis to establish the appropriate X-Factor(s) for the elective price cap LECs.

Respectfully submitted,

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Dated: September 3, 1997

CERTIFICATE OF SERVICE

The undersigned hereby certifies that copies of Cincinnati Bell Telephone Company's Reply to Opposition to its Petition for Reconsideration of the Fourth Report and Order have been sent by first class United States Mail, postage prepaid, or by hand delivery, on September 3, 1997, to the persons listed on the attached service list.


Judy Piepmeier

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